AMENDED IN ASSEMBLY MAY 2, 2011

CALIFORNIA LEGISLATURE—2011–12 REGULAR SESSION

ASSEMBLY BILL No. 1408

Introduced by Committee on Banking and Finance (Assembly Members Eng (Chair), Achadjian (Vice Chair), Fletcher, Gatto, Roger Hernández, Lara, Perea, and Torres)

March 9, 2011

An act to amend ~~Section 16731~~ *Sections 16731 and 16731.5* of the Government Code, relating to general obligation bonds.

LEGISLATIVE COUNSEL'S DIGEST

AB 1408, as amended, Committee on Banking and Finance. General obligation bonds.

The State General Obligation Bond Law generally provides for a procedure that may be adopted by other acts, with any necessary modifications, to authorize the issuance and sale of state general obligation bonds, *including general obligation bonds to be issued as zero coupon or capital appreciation bonds,* and to provide for the repayment of those bonds. Existing law requires, with regard to a resolution determining that the sale of all or part of the bonds is necessary or desirable, a specification that the denomination of the bonds to be sold shall be $1,000 or multiples of that sum.

This bill would instead require a specification that the denomination of the bonds to be sold shall be $25 or multiples of that sum.

Vote: majority. Appropriation: no. Fiscal committee: yes. State-mandated local program: no.

The people of the State of California do enact as follows:

SECTION 1. Section 16731 of the Government Code is amended to read:

16731. Whenever the committee determines that the sale of all or any part of the bonds authorized to be issued is necessary or desirable, it shall adopt a resolution to that effect. The resolution shall specify all of the following as to the bonds then to be sold:

(a) The aggregate number, aggregate par value, denominations, and the date of the bonds to be then sold. The denominations shall be in the sum of twenty-five dollars ($25) or multiples of that sum. The date appearing on the bonds shall be deemed to be the date of issuance for all purposes of this chapter, irrespective of the actual date of delivery of the bonds and the payment of the purchase price of the bonds.

(b) The dates of maturity and the amount of the bonds maturing at each date of maturity, which amounts need not be equal. The last dates of maturity shall be not more than 45 years after the date of the bonds.

(c) Whether or not the bonds are to be subject to redemption or tender prior to maturity, and, if so, the provisions for the redemption or tender, the manner of the call or notice thereof, and the price or prices at which the bonds shall be subject to redemption or tender.

(d) (1) (A) The annual rate, or rates, of interest that the bonds to be issued shall bear, which shall be in the increments determined by the Treasurer, but not in excess of 11 percent. The rate or rates may be determined at the time of the sale of the bonds.

(B) As an alternative to subparagraph (A), the resolution may specify that the bonds may pay a variable interest rate or rates, as prescribed in the resolution, but not in excess of 11 percent per annum, and in accordance with the requirements of this subparagraph.

(i) At the time and as the result of the issuance of any bonds bearing a variable interest rate, the aggregate principal amount of all state general obligation bonds bearing variable interest rates may not exceed 20 percent of the aggregate principal amount of all state general obligation bonds then outstanding.

(ii) For purposes of the calculation made pursuant to clause (i), variable rate bonds shall not include commercial paper notes issued pursuant to Section 16731.6 or bonds that have an effective fixed interest rate through a hedging contract, as specified in subparagraph (C), but shall include bonds that have an effective variable interest rate through a hedging contract.

(iii) Notwithstanding any other provision of this chapter, if the committee decides to issue state general obligation bonds bearing variable interest rates, the committee is not required to comply with Section 16732.

(iv) Notwithstanding any other provision of law, if bonds are issued bearing a variable interest rate under a bond act approved by the voters on or after January 1, 2002, and if the variable interest rate bonds provide a right of tender, then any amount payable by the state as a result of the tender with respect to principal of and interest on the bonds prior to the regularly scheduled principal or interest payment dates, or payable by the state pursuant to redemption or call initiated as a means to repay the obligation of the state resulting from the tender, is backed by the full faith and credit of the state and shall be payable under the bond act.

(v) A contractual obligation of the state to repay advances and pay interest thereon under a credit enhancement or liquidity agreement entered into in connection with variable interest rate bonds providing a right of tender and issued under a bond act approved by the voters on or after January 1, 2002, shall be backed by the full faith and credit of the state and shall be payable under the bond act, except to the extent bond interest paid with an advance and interest on the advance would exceed the maximum interest rate specified in this subdivision.

(C) For the purposes of clause (ii) of subparagraph (B), bonds that have an “effective fixed interest rate through a hedging contract” means bonds for which the Treasurer determines the hedging contract meets either of the following conditions:

(i) Significantly reduces variable rate risk by providing changes in fair values or cashflows that substantially offset the changes in fair value or cashflows of the bonds.

(ii) Qualifies for integration with the bonds in calculating the yield on the bonds under the rules prescribed in Section 148 of the United States Internal Revenue Code (26 U.S.C. Sec. 148).

(D) The Treasurer’s determination specified in subparagraph (C) shall be made at the time the hedging contract is entered into and shall apply through the maturity of the bonds, unless the hedging contract is terminated prior to maturity.

(2) (A) (i) Notwithstanding any other provision of law, for bonds approved by the voters after January 1, 2006, payment of any amounts owed by the state to a counterparty, after any offset for payments owed to the state on any hedging contract described in Section 5922 in connection with those bonds, shall be deemed to be included within the appropriation for interest on the bonds contained in the applicable bond act.

(ii) The total payments of stated interest on the bonds together with payments owed by the state after any offset for payments owed to the state on a hedging contract shall not exceed the maximum interest rate set forth in this subdivision.

(iii) To the extent payments of interest on a bond, together with payments on a hedging contract, would, in any fiscal year, exceed the maximum interest rate specified in this subdivision, the excess amounts may be paid in subsequent fiscal years, if the aggregate amount of interest and that excess amount paid in any year does not exceed the maximum interest rate specified in this subdivision.

(B) The Treasurer may not enter into any hedging contract described by subparagraph (A) unless the committee has approved policies developed by the Treasurer relating to the entering into and managing of those hedging contracts that shall include both of the following:

(i) A requirement that any hedging contract or program of contracts is designed to reduce the amount or duration of payment, currency, rate, spread, or similar risk or result in a lower cost of borrowing when used in combination with the issuance or carrying of bonds.

(ii) A description of the criteria to be used to evaluate the potential risks and benefits to the state of entering into a particular hedging contract or program of contracts and to evaluate the performance of outstanding hedging contracts in comparison to the objectives for which the hedging contract was executed.

(C) The policies approved pursuant to subparagraph (B) are exempt from the requirements of Chapter 3.5 (commencing with Section 11340) of Part 1 of Division 3.

(e) The interest payment dates.

(f) The technical form and language of the bonds.

(g) Whether or not the right is reserved to make delivery in the form of temporary or interim bonds, certificates, or receipts, exchangeable for definitive bonds when executed and available for delivery. If the right is reserved, the denominations and form of the temporary securities shall be stated.

(h) Provisions for the registration and exchange of bonds and for the use of a depository to hold book-entry bonds after issuance.

(i) All other terms and conditions of the bonds and of the execution, issuance, and sale of the bonds, which shall be consistent with all of this chapter.

SEC. 2. Section 16731.5 of the Government Code is amended to read:

16731.5. (a) Notwithstanding any other provision of this chapter, the committee may provide for the issuance of all or part of the bonds authorized to be issued as zero coupon or capital appreciation bonds. The committee shall adopt a resolution finding that issuance of these bonds is necessary and desirable, directing the Treasurer to arrange for preparation of the requisite number of suitable bonds, and specifying other provisions relating to the bonds including the following:

(1) The date, number, denominations, and aggregate par value of the bonds payable at maturity. The aggregate par value may be represented by bond certificates in denominations as the committee deems appropriate, but not less than ~~one thousand dollars ($1,000)~~ *twenty-five dollars ($25)*.

(2) The dates of maturity and the aggregate amounts of the bonds maturing on each of these dates. Determination of maturity dates and amounts by the committee shall be made upon recommendation of the Treasurer to provide the maximum benefit to potential purchasers and to respond to the expected demand for the bonds. Whenever the committee determines to issue bonds from any authorized bond act as zero coupon or capital appreciation bonds, and to issue bonds from the same authorization at the same time pursuant to Section 16731, the committee may comply with the requirements of subdivision (b) of Section 16731 by taking into account all the bonds of the same authorization being issued at the same time.

(3) The interest rate or rates, and interest payment dates applicable to the bonds. Zero coupon bonds may bear a zero rate of interest, and capital appreciation bonds may bear a stated rate

of interest payable only at maturity, compounded at the same rate, which rate or rates may be determined at the time of sale of the bonds. The rate of interest borne by these bonds, or the nominal interest rate taking into account the original issue discount of these bonds, when bearing a zero interest rate, shall not exceed 11 percent per annum.

(4) Any provisions for the redemption of the bonds prior to their stated maturity.

(5) The technical form and language of the bonds.

(6) All other terms and conditions of the bonds and of their execution, issuance, and sale, deemed necessary and appropriate by the committee.

(b) Notwithstanding any other provision of this chapter, when the committee determines to issue bonds as zero coupon or capital appreciation bonds, all of the following shall apply:

(1) The bonds may be sold at negotiated sale at a price below the par value in a manner consistent with paragraph (3) of subdivision (a). If the committee determines to issue other bonds authorized by the same bond act at the same time as zero coupon or capital appreciation bonds are issued, the other bonds may also be sold at negotiated sale with a discount of not more than 3 percent of the par amount thereof.

(2) For purposes of determining the principal amount of bonds of any voted authorization outstanding, in the case of any bonds which are zero coupon or capital appreciation bonds and do not provide for payment of interest on the bond prior to maturity, the principal amount of the bonds shall be the cash price paid by the initial purchasers of the bonds to the state, and deposited in the fund, plus the amount of any costs of issuance of the bonds. Within 30 days of the delivery of any zero coupon or capital appreciation bonds, the Treasurer shall submit to the committee a certificate stating the principal amount of bonds of each issue, calculated as stated in this subdivision, which have been sold, and the certification shall be conclusive for all purposes under this chapter and the constitution.

(3) The committee may arrange to utilize the services of investment banks, commercial banks, savings and loans or other financial institutions, or other advisers as it may deem appropriate to publicize and assist in the marketing and sale of zero coupon or capital appreciation bonds.

(c) When zero coupon or capital appreciation bonds are issued pursuant to this section, the debt service payments on the bonds should continue to be managed in a manner consistent with the state's policy of retiring general obligation bonds in an orderly efficient manner. It is the expectation of the Legislature that the authority provided by this section will not be used to defer debt service payments as a means of preserving General Fund moneys for short-term purposes. The committee shall provide in the resolution authorizing the issuance of zero coupon or capital appreciation bonds that the state shall set aside, in a separate trust fund within the State Treasury, an amount in each year representing the amount of interest accrued during that year to be payable at the maturity of the bonds, with these payments to be deemed a payment of debt service on the bonds.

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